STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition of PAUL D. JAFFE for Revision of a Determination or for Refund of Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law.	:	DETERMINATION DTA NOS. 811953 AND 811987
In the Matter of the Petition of LEON J. GREENSPAN for Revision of a Determination or for Refund of Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law.	:	

Petitioner Paul D. Jaffe, 180 East Post Road, White Plains, New York 10601, filed a petition for revision of a determination or for refund of tax on gains derived from certain real property transfers under Article 31-B of the Tax Law.

Petitioner Leon J. Greenspan, 14 Pinebrook Drive, White Plains, New York 10605, filed a petition for revision of a determination or for refund of tax on gains derived from certain real property transfers under Article 31-B of the Tax Law.

A hearing was held before Catherine M. Bennett, Administrative Law Judge, at the offices of the Division of Tax Appeals, Riverfront Professional Tower, 500 Federal Street, Troy, New York, on March 21, 1994 at 1:15 P.M., with all briefs to be submitted by August 5, 1994, including a short extension of time granted to the parties. Petitioner Leon J.Greenspan appeared pro se. The Division of Taxation appeared by William F. Collins, Esq. (Andrew J. Zalewski, Esq., of counsel).

Petitioner Paul D. Jaffe consented to have the controversy determined on submission

without hearing. Petitioner and the Division of Taxation's representative, on March 31, 1994 and April 11, 1994, respectively, agreed to the submission of the matter as it pertained to Mr. Jaffe. Both petitioners agreed that a consolidated determination shall be issued since the facts of the matter equally apply to them. Petitioner Paul D. Jaffe submitted a brief which was received by the Division of Tax Appeals on May 27, 1994 on behalf of both petitioners. The Division of Taxation submitted a brief on July 11, 1994. Thereafter, petitioners submitted no reply brief and the record of this matter was deemed closed on August 5, 1994.

ISSUES

I. Whether, upon conveyance of an interest in real property, it was proper for the Division of Taxation to aggregate the consideration received by petitioners, who held their interest in the property as tenants-in-common, with the interests of other transferors who were also tenants-in-common, in order to determine the applicability of the $1,000,000.00 exemption from real property gains tax.

II. Whether the Division of Taxation properly determined that petitioners' primary purpose for the transfers in issue was avoidance or evasion of the tax imposed by Article 31-B of the Tax Law, allowing the Division of Taxation an additional basis to treat such transfer as subject to tax.

FINDINGS OF FACT

Petitioners, Paul D. Jaffe and Leon J. Greenspan, were limited partners in a partnership known as Gadlex Associates ("Gadlex"). Gadlex's sole asset was fee ownership of an office building located at 180 East Post Road, White Plains, New York ("the property").

Relevant to this matter, the Gadlex partners and their interests in the partnership's property were as follows:

Partner	Percentage of Interest in Gadlex
Paul D. Jaffe	27½%
Leon J. Greenspan	27½%
Herbert K. Kanarek	30 %
Joel Martin Aurnou	15 %

As a result of litigation involving Gadlex and its four partners, an interlocutory

judgment dated October 26, 1990 was rendered in Supreme Court of the State of New York, Westchester County, ordering the assets of the partnership to be sold and liquidated at a partition sale by auction on or before March 6, 1991. A receiver was appointed for the purpose of administering the assets of Gadlex and to conduct the auction. The proceeds from the sale of assets were to be used to discharge the obligations of Gadlex and the remaining proceeds were to be distributed to the limited partners. The judgment by its terms set forth the partnership interests of each partner and was structured such that if any partner were the successful bidder, the effect thereof was to set a value on that building for the purpose of the successful partner or partners buying out the remaining persons. A public auction was held on March 12, 1991 and, as a result, partners Mr. Kanarek (with an interest of 30%) and Mr. Aurnou (with an interest of 15%) were the successful purchasers buying out Mr. Greenspan and Mr. Jaffe (with a collective interest of 55%) at a bid value of $1,250,000.00. Mr. Greenspan and Mr. Jaffe were to receive, in the aggregate, 55% of that value, or $687,500.00 less certain adjustments for partnership obligations. The judgment also provided that if any of the partners were successful bidders, they could apply their partnership interest against the bid price and needed only to pay over directly to the remaining partners their partnership interest based on such price. The successful purchasing partners, Mr. Kanarek and Mr. Aurnou (with a combined partnership interest of 45%) were originally going to assign their bid to a newly-formed partnership known as Post 180 Associates. They intended that their capital contribution to the partnership would be their 45% Gadlex partnership interest credit plus a prorated share of additional working capital to be advanced by all the partners in the new partnership. In return they would own a collective 45% interest in Post 180 Associates.

Transferor and transferee questionnaires were filed dated July 22, 1991 and July 17, 1991, respectively, reporting an anticipated transfer of the property by Gadlex to Post 180 Associates (Exhibit "Y"). The transferee questionnaire identified Gadlex as the transferor and Post 180 Associates, Mr. Aurnou and Mr. Kanarek as the transferees. The date of anticipated transfer was August 1, 1991 and on the questionnaire the "consideration to be paid to transferor

by transferee" was equal to $687,500.00. Based on such information, the Division of Taxation ("Division") issued a tentative assessment to Gadlex on October 31, 1991 computing tax of $40,325.03 owed with respect to the transfer of the property (Exhibit "X"). The explanation and calculation of anticipated tax due provided by the Division stated the following:

> "Section 590.50(c) of the Gains Tax Regulations provides that in cases where a transfer consists of a partial mere change of identity or form of ownership or organization 'the million-dollar exemption is applied to consideration first and then the mere change exemption is applied. A transfer in which the consideration is greater than $1 million will remain taxable; the mere change exemption only defers payment of tax on the portion of gain determined to be attributed to a mere change in form of ownership.'
>
> "Since the consideration for the transfer before applying the 45% mere change exemption is over $1 million, the exemption claimed under Section 1443.1 of the Tax Law for a transfer where the consideration is less than $1 million has been denied.
>
> "The anticipated tax due was computed as follows:

Consideration		$1,250,000.00
Original purchase price		(516,817.65)
Gain		$733,182.35
% Change of owenrship [sic]		x 55%
Gain subject to tax (net adjustments)	$403,250.29	
Tax @10%		$40,325.03"

After additional conflict among the partners, the transaction was restructured. Upon the dissolution of Gadlex, the partnership property was distributed in kind to the limited partners according to their respective percentages, with the former limited partners then owning the property as tenants-in-common. On or about January 23, 1992, petitioners and Post 180 Associates entered into an agreement which provided Post 180 Associates an option to buy the undivided tenancies-in-common from each of the petitioners. Such options were required to be exercised on or before February 17, 1992.

A final judgment arising out of the litigation concerning the Gadlex dissolution was entered on March 16, 1992. In pertinent part, it declared that the interlocutory judgment dated October 26, 1990 be vacated and set aside and that the directive in such decision, i.e., the order for the auction sale, also be vacated. In addition, the final judgment stated that the auction sale conducted pursuant to the authority of the interlocutory judgment be declared to be a nullity. It

was further decreed that the limited partnership of Gadlex terminated effective February 27, 1990 and that partnership interests of the limited partners of Gadlex were distributed in kind to them such that each of the limited partners would hold his individual distributed share as a tenant-in-common according to the percentages described in Finding of Fact "2". In proportion to their partnership interests, each of the limited partners was also required to pay certain of the partnership obligations.

Essentially, the restructured deal would convey the subject property to the new limited partnership known as Post 180 Associates in three transactions. The first transaction resulted from the eventual dissolution of Gadlex and an in-kind distribution of the subject property to the limited partners in their respective interests. The Division determined that this transaction was a mere change of identity and issued a tentative assessment providing for no gains tax due.

The second transaction reflected the conveyances by Mr. Kanarek and Mr. Aurnou of their collective 45% interest as tenants-in-common to Post 180 Associates in return for their respective 30% and 15% partnership interests in Post 180 Associates. The Division again determined this transaction to be a mere change of identity and, as to Mr. Kanarek and Mr. Aurnou, waived any gains tax liability.

The third transaction reflected the purchase of petitioners' collective 55% interest as tenants-in-common of the property by Post 180 Associates for a combined consideration of $687,500.00. The Division aggregated this transaction with the consideration from the second transaction above to determine the $1,000,000.00 threshold. It did so on the basis that the original bid price on the property was $1,250,000.00. Since the transaction then exceeded the $1,000,000.00 threshold, the Division determined a portion of the transaction was subject to gains tax and assessed petitioners collectively $40,325.03.

On February 3, 1992, the Division received entirely revised sets of transferor and transferee questionnaires from petitioners and the other limited partners. The transferee questionnaires filed with respect to the transfer from Mr. Kanarek and Mr. Aurnou to Post 180 Associates indicated that the "consideration to be paid to transferor by transferee" was equal to

zero. As to the transferee questionnaires filed with respect to the transfer by Mr. Greenspan and Mr. Jaffe to Post 180 Associates, the "consideration to be paid to transferor by transferees" was $687,500.00.

A schedule of adjustments dated February 18, 1992 and completed in conjunction with the tentative assessment and return provided the following explanation:

> "In applying the $1 million exemption, Tax Law Section 1440.7 provides for the aggregation of consideration received on the transfer of real property by tenants in common, joint tenants or tenants by the entirety. Since the consideration ($687,500.00) for the transfer of L.J. Greenspan's [and] P.D. Jaffe's combined 55% tenant in common interest in the property plus the consideration ($562,500.00**) for the transfer of the remaining 45% tenant in common interests exceeds $1 million, the exemption claimed under Tax Law Section 1443.1 is denied. The anticipated tax due was computed as follows:
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> | | | |
> |---|---|---|
> | Consideration for combined 55% tenant in common interests of L.J. Greenspan and P.D. Jaffe. | $687,500.00 | |
> | Original purchase price attributable to combined 55% tenant in common interests ($516,817.65 x 55%) | | (284,249.71) |
> | Gain subject to tax (Net Adjustments) | 403,250.29 | |
> | Tax @10% | | 40,325.03 |
>
> "** Although not subject to tax by virtue of the mere change exemption applied, the consideration for the transfer of the 45% tenant in common interest was determined by the value of the partnership interest in Post 180 Associates received for the transfer."

Petitioners paid the tax due and filed claims for refund of their respective shares. The basis for the refund claim was that the consideration received was less than $1,000,000.00.

On July 30 and 31, 1992, petitioners were issued correspondence from the Division denying the refund claim of each petitioner. The reasoning is identical and the content, in pertinent part, is provided below:

> "Claimant contends that the subject transfer should be exempt from gains tax because the consideration received does not meet the $1 million threshold.
>
> "A review of our files shows that Gadlex Associates a limited partnership was fee owner of the subject property. In February 1992 the partnership dissolved and ownership of the property transferred to the four limited partners as tenants in common based on their percentage of ownership.
>
> "Two of the tenants in common, Kanarek and Aurnou, then conveyed their interests to a new limited partnership, Post 180 Associates. At that time the partners of Post

180 Associates bought out the remaining two tenant in common interests of Paul Jaffe and Leon Greenspan.

"Section 590.43(d) of the Gains Tax Regulations provides that when several transferors, owning one parcel of land as tenants in common transfer their interests to one transferee the consideration paid to each such transferor be aggregated with the consideration paid to the other transferors in determining whether the consideration is $1 million or more. Once the million dollar threshold is met, each transferor is liable for payment of tax based on the consideration he receives, less his original purchase price of the property.

"Also, Regulation Section 590.50(c) states that the million dollar exemption is applied to consideration first and then the mere change exemption is applied. A transfer in which the consideration is greater than $1 million will remain taxable, the mere change exemption only defers payment of tax on the portion of gain attributed to a mere change in form of ownership.

"Therefore, it is our position that the consideration received by claimant for the transfer of his interest in the subject property to Post 180 Associates must be aggregated with the consideration received by the remaining three tenants in common for the transfer of their interests in Post 180 Associates.

"Since the aggregate consideration exceeds $1 million the consideration received by claimant is subject to tax less his original purchase price of the property.

"Accordingly, the refund claim of [petitioners] is hereby denied in its entirety." (Exhibits "B" and "H".)

The Bureau of Conciliation and Mediation Services received timely requests for conciliation conference from both petitioners on August 24, 1992. A conciliation conference was conducted on January 7, 1993 and conciliation orders were issued to each petitioner, dated April 16, 1993, denying their refund claims. Timely petitions were filed with the Division of Tax Appeals by Mr. Jaffe and Mr. Greenspan on June 9, 1993 and June 17, 1993, respectively.

The question in this matter concerns what, if any, consideration was received by Mr. Kanarek and Mr. Aurnou on their transfer of their 45% collective interest as tenants-in-common of the property to Post 180 Associates, and whether the Division appropriately aggregated such transfers with those of petitioners.

SUMMARY OF THE PARTIES' POSITIONS

Petitioners maintain that the consideration received by them is less than $1,000,000.00 and thus it qualifies as an exempt transaction. Petitioners assert that the transfer of the interests owned by the other tenants-in-common was without consideration and, as such, should not be

aggregated with petitioners' interests in determining consideration. Since the transfer of the other tenants-in-common was an exempt transaction as consisting of a "mere change of identity or form of ownership", petitioners claim that implicit in such definition is the absence of consideration. Accordingly, since there was less than $1,000,000.00 of consideration, petitioners' refund of real property gains tax paid in this matter should be granted. As to tax avoidance, petitioners take the position that a taxpayer has the right to reduce or avoid taxes by any means which the law permits, citing pertinent authority.

The Division asserts that it properly aggregated the "consideration" received by all the tenants-in-common who held an interest in 180 East Post Road since the term "consideration" also refers to "any other thing of value." The Division maintains that it is only after consideration is determined that the mere change in identity exemption is allowed to be applied. Accordingly, the Division believes that it properly aggregated the consideration received by the four tenants-in-common resulting in consideration of $1,000,000.00 or more, thereby subjecting the transfers of petitioners to taxation regardless of exemptions that may have applied to other tenants-in-common. As to the tax avoidance issue, the Division asserts that petitioners have provided no business purpose for the transfer in question and alleges that such transfer was formulated with the primary purpose being to avoid payment of real property gains tax and, as such, is not allowed.

CONCLUSIONS OF LAW

A. Tax Law § 1441 imposes a tax at a rate of 10% upon gains derived from the transfer of real property within New York State. Certain exemptions from the tax are provided for in Tax Law § 1443. One such exemption is that no tax shall be imposed if the consideration is less than $1,000,000.00 (Tax Law § 1443[1]). Generally, statutory exemptions from tax are strictly construed, and the taxpayer must clearly establish that he is entitled to the claimed exemption (see, Matter of Lever v. New York State Tax Commn., 144 AD2d 751, 535 NYS2d 158).

B. The term "transfer of real property" is defined in Tax Law § 1440(7) which provides,

in part, as follows:

> "'[t]ransfer of real property' means the transfer or transfers of any interest in real property by any method, including but not limited to sale . . . ."

C. The third sentence of Tax Law § 1440(7) is known as the "aggregation clause". It provides:

> "[t]ransfer of real property shall also include partial or successive transfers, unless the transferor or transferors furnish a sworn statement that such transfers are not pursuant to an agreement or plan to effectuate by partial or successive transfers a transfer which would otherwise be included in the coverage of this article, and the transfer of real property by tenants in common, joint tenants or tenants by the entirety, provided that the subdividing of real property and the sale of such subdivided parcels improved with residences to transferees for use as their residences, other than transfers pursuant to a cooperative or condominium plan, shall not be deemed a single transfer of real property."

D. The aggregation clause has a bearing upon the application of the $1,000,000.00 exemption because when the proceeds from the transfer are treated as a single transaction, they are aggregated in order to determine whether the exemption is applicable (see, Matter of Lee, Tax Appeals Tribunal, October 15, 1992, confirmed 202 AD2d 924, 610 NYS2d 330).

E. The pertinent portion of the aggregation clause is explained in the Commissioner's regulation at 20 NYCRR 590.43(d) which states:

> "Question: How is the aggregation clause of section 1440(7) of the Tax Law . . . applied in the case of:
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> * * *
>
> "(d) Several transferors, owning one parcel of land either as joint tenants, tenants in common, or as tenants by the entirety, one transferee?
>
> "Answer: The statute specifically requires that the consideration paid to each such transferor be aggregated with the consideration paid to the other transferors in determining whether the consideration is $1 million or more. Once the million-dollar threshold is met, each transferor is liable for payment of tax based on the consideration he receives, less his original purchase price for the property" (emphasis added).

F. It has been observed that the foregoing regulation sets forth the principle that when determining the applicability of the $1,000,000.00 exemption, the pertinent inquiry is the total consideration paid for the jointly-owned property (Matter of Lee, supra). The term "consideration", as defined by Tax Law § 1440(1)(a), includes, in pertinent part, "any price paid

or required to be paid, whether expressed in a deed and whether paid or required to be paid by money, property, or any other thing of value . . . ."

A particular party's proportionate interest in the proceeds only has a bearing on that individual's liability for the gains tax due on the transaction (Matter of Lee, supra).

G. The pertinent portion of 20 NYCRR 590.50 provides guidance on the "mere change of identity" exemption as follows:

> "(a) Question: Section 1443(5) of the Tax Law exempts a transfer from the gains tax to the extent it 'consists of a mere change of identity or form of ownership or organization, where there is no change in beneficial interest.' Does this exempt:
>
> "(1) The transfer of real property by a person to a partnership in exchange for an interest in the partnership?
>
> "Answer: Yes. Partially. This is a mere change in the form of ownership and would be exempt to the extent of the person's interest in the partnership."
>
> * * *
>
> "(c) Question: How does the mere change of identity exemption interrelate with the million-dollar exemption?
>
> "Answer: The million-dollar exemption is applied to consideration first and then the mere change exemption is applied. A transfer in which the consideration is greater than $1 million will remain taxable, the mere change exemption only defers payment of tax on the portion of gain determined to be attributed to a mere change in form of ownership."

H. Applying the foregoing principles to the facts of this case leads to the conclusion that petitioners are liable for the gains tax in issue. Petitioners concede that they received the combined sum of $687,500.00 for their interests in the property in question, each having a 27½% tenant-in-common interest in the property. However, petitioners maintain that, without question, the consideration received is less than $1,000,000.00, making the transaction eligible for the $1,000,000.00 exemption since the transfers of Mr. Kanarek and Mr. Aurnou to Post 180 Associates was without consideration. General partnership principles dictate a different result.

New York law provides that a partnership's capital consists of the sums contributed by its members for the purpose of commencing or carrying on the partnership business and intended to be risked in the business (15 NY Jur 2d, Business Relationships, § 1329). The basic capital accounting rules of Internal Revenue Code § 704 and attendant regulations require that a

partner's capital account be increased by the fair market value of property contributed to the partnership by such partner on the date of contribution (Treas Reg § 1.704-1[b]). The capital account bears a book value which is equal to the fair market value at the time of contribution and the book value is initially the value used in determining the contributing partner's capital account and is adjusted thereafter for cost recovery and other events that affect the basis of the property (Treas Reg § 1.704-3[a][3][i]).

Each of the four tenants-in-common effectuated a transfer of the property in issue. The two partners who received a partnership interest in Post 180 Associates received value to the extent of the fair market value of the property at the time of contribution. The parties do not dispute the value placed on the property at $1,250,000.00 and distributed such property in accordance with such value. Clearly, the "thing of value" which Mr. Kanarek and Mr. Aurnou received was their interest in the partnership at a value of $562,500.00. When added to the consideration paid to petitioners in cash of $687,500.00, the total consideration received for the transfers by such tenants-in-common exceeded $1,000,000.00, and since a transfer in which the consideration is greater than $1,000,000.00 remains taxable, the mere change exemption will only defer payment of tax on that portion of the gain determined to be attributable to a mere change in form of ownership (20 NYCRR 590.50[c]). As such principles apply to this case, the Division properly denied the refund claims of petitioners herein.

I. The Division asserts that if it is determined that any transfer of real property or interest in such property has been formulated such that the primary purpose is the avoidance or evasion of tax imposed by Article 31-B rather than for an adequate business purpose, the Division shall treat such transfer as subject to gains tax (Tax Law § 1448[1]). Certainly there is a fine line between the planning of a transaction, taking into consideration the taxation of such transaction and the avoidance or evasion of such tax. This case is not absent an implication that the parties attempted to restructure the deal for reasons of reducing any potential gains tax liability. However, for other reasons as well, including the ongoing dispute among the limited partners, the original auction was never concluded. Attached to the final judgment was a stipulation by

the parties to that litigation which spoke to the "comprehensive resolution of the issues in this partnership dissolution proceeding." Further, annexed is the report of the receiver which makes reference to the fact that although he conducted the auction sale in March 1991, the transaction was never concluded and was now being replaced by what became the final judgment. He also stated that it was a settlement of the issues between the partners "particularly in relation to resolving issues raised regarding certain credits against rent . . . allowed to petitioners." It appears as though the purpose behind the restructuring was somewhat mixed in motive such that it is determined herein that Tax Law § 1448(1) in and of itself is insufficient to hold petitioners liable for gains tax. In other words, the presence of the final judgment, stipulation and report of receiver, though not specific with regard to intent, provide some indication that there were business and litigation settlement motives additionally involved with respect to the ultimate restructuring of the transactions herein. Accordingly, it cannot be held that the primary purpose for the transfers in issue is the avoidance or evasion of gains tax.

J. The petitions of Paul D. Jaffe and Leon J. Greenspan are denied and the denial of the refund claims is hereby sustained.

DATED: Troy, New York
February 2, 1995

/s/ Catherine M. Bennett
ADMINISTRATIVE LAW JUDGE